

# FISCAL NOTE

**Bill #:** HB0276

**Title:** Property tax surtax on certain residences for state emergency services

**Primary Sponsor:** Jacobson, H

**Status:** As Introduced

Sponsor signature

Date

David Ewer, Budget Director

Date

## Fiscal Summary

	<b><u>FY 2006 Difference</u></b>	<b><u>FY 2007 Difference</u></b>
<b>Expenditures:</b>		
General Fund	\$761,364	\$592,182
<b>Revenue:</b>		
General Fund	(\$761,364)	\$20,000,000
<b>Net Impact on General Fund Balance:</b>	(\$761,364)	\$19,407,818

- |   |   |
|---|---|
| <input type="checkbox"/> Significant Local Gov. Impact    | <input checked="" type="checkbox"/> Technical Concerns            |
| <input type="checkbox"/> Included in the Executive Budget | <input checked="" type="checkbox"/> Significant Long-Term Impacts |
| <input type="checkbox"/> Dedicated Revenue Form Attached  | <input checked="" type="checkbox"/> Needs to be included in HB 2  |

## Fiscal Analysis

### ASSUMPTIONS:

1. This bill provides that if the owner of a single-family residence has not paid Montana individual income taxes in the prior year, then the taxpayer will pay a 20 percent surtax on the residential property for the current year to defray the provision of state emergency services to the property. All proceeds from the surtax are deposited in the state general fund.
2. Specifically, the bill provides that the surtax applies if the owner of the property “has not paid income taxes under 15-30-103, MCA, in the prior year”. For the purposes of the revenue impact shown on this fiscal note, this is assumed to mean that the property owner is subject to the 20 percent surtax if the taxpayer had no positive income tax liability for the tax year. All people who own a residence in Montanans and pay residential property taxes, but who have no individual income tax liability for the prior year would be subject to the surtax, regardless of whether an income tax return was filed or not.
3. Taxpayers who did not pay individual income taxes in the prior year because of age, infirmity, or misfortune are exempt from paying the surtax.
4. This proposal applies to property tax years beginning after December 31, 2005. This is assumed to mean that property tax bills will be subject to the surtax in tax year 2006 if the taxpayer did not pay income taxes in tax year 2005. Tax bills for tax year 2006 are paid in November of 2006 and May of 2007, so the earliest that this proposal will impact the general fund is FY 2007.

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5. In tax year 2003 residential property taxes totaled \$402 million. Of this amount, approximately \$260 million was taken as an itemized deduction on individual income tax returns where some individual income tax was paid. An additional \$24 million was paid by elderly taxpayers who also filed for the elderly homeowner/renter credit. These property taxes would not be subject to the surtax, leaving a balance of \$118 million. Of this amount, surtaxes would not be payable for 1) taxpayers who are not residents of the state, but paid some state income tax on income attributable to Montana; 2) taxpayers who paid income taxes and own residential property but took the standard deduction, rather than itemizing deductions; and 3) taxpayers who own single-family residences but who rent those properties to other taxpayers. It is assumed that these taxpayers account for an additional \$18 million in property taxes that would not be subject to the surtax. This leaves a balance of about \$100 million in property taxes associated with taxpayers who paid no individual income tax in the prior year.
6. Based on the above assumption, it is estimated that this bill would raise approximately \$20 million annually (\$100 million X 20% surtax = \$20 million).
7. Administrative costs associated with the enforcement of the provisions of this bill, and to ensure compliance with the law would be significant. The Department estimates that additional administrative expenses would total \$761,364 in FY 2006, and \$592,182 in FY 2007. This includes the addition of 16.5 FTE, grade 8 property valuation specialists, in each year, primarily to provide for the cross-matching process between residential properties and individual income tax filing to ensure compliance with the program. There would also be costs associated with a taxpayer education program; updating department computer systems to provide for tracking of property owners that have or have not paid income tax, and property becomes subject to the surtax; upgrades to county computer systems to provide for the proper billing of property taxes, including the surtax; data entry; and form printing and mailing.

### FISCAL IMPACT:

	FY 2006 <u>Difference</u>	FY 2007 <u>Difference</u>
FTE	16.5	16.5
<u>Expenditures:</u>		
Personal Services	\$417,344	\$416,119
Operating Expenses	245,420	176,063
Equipment	<u>98,600</u>	<u>0</u>
TOTAL	\$761,364	\$592,182
<u>Funding of Expenditures:</u>		
General Fund (01)	\$761,364	\$592,182
<u>Revenues:</u>		
General Fund (01)	\$0	\$20,000,000
<u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u>		
General Fund (01)	(\$761,364)	\$19,407,818

### LONG-RANGE IMPACTS:

This proposal would continue to provide additional general fund revenues on the order of \$20 million annually, and the increased associated administrative expenses discussed above.

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### TECHNICAL NOTES:

1. The surtax is 20 percent of the property taxes payable. It is unclear what the surtax would be based and levied upon. It is unclear whether the surtax would be levied upon:
  - a. Only the state mill levies (95 mills for school equalization and the university 6 mill);
  - b. all property taxes based on mill levies including local government and school mills; or
  - c. in addition to all property taxes based on mill levies, would the surtax be levied upon property related fees like special interest districts (SID's) fees (street maintenance, fire hydrant, lighting, garbage, weed, water, sewer districts, etc.)?
2. American Indians living on reservation fee lands pay property taxes, but may not be required to pay individual income taxes by state or federal law. This bill would add a 20 percent surtax to the property taxes of certain American Indians because they did not pay income taxes in the prior year, even though they may have had no legal obligation to pay income taxes. Language could be added to the bill providing that property taxpayers who for whatever reason are not subject by law to state individual income taxes would not be subject to the property tax surtax.
3. There are thousands of farmsteads organized as sole proprietorships, partnerships or other forms of pass-through entities that are subject to individual income taxes. Generally speaking, current accounting practices and rules result in many of these farms from having to pay individual income taxes. The property taxes on the residential portion of these farmsteads would be subject to the 20 percent property tax surtax in each year following a year in which the farm operation showed a net loss.
4. In order to provide for the effective administration of this proposal, particularly with respect to ensuring compliance with the specific provisions of this bill, the Department of Revenue must have the capability of cross-matching individual income tax returns with property tax records. Currently, no such ability exists. Given the current state of database development, there is no way of determining if a particular owner of residential property did or did not pay individual income taxes in the previous year. Enforcement of this proposal would be extremely difficult; particularly in cases where the residential property is owned by a sole proprietorship or some form of pass-through entity for which the residential property taxes are taken as a business expense deduction, rather than reported as an itemized deduction on the individual taxpayer's return.
5. Individuals owning residential property, but with incomes below the filing thresholds for individual income tax purposes would be subject to the 20 percent surtax on their residential property tax each year.
6. The bill provides that taxpayers are exempt from the surtax because of "age, infirmity, or misfortune", but does not define what these terms mean. Providing a more precise definition would greatly facilitate administration of the provisions of this bill.
7. The bill provides that the surtax applies to taxpayers who have not "paid income taxes under 15-30-103 in the prior year." If a taxpayer files an income tax return for the prior year, and calculates his liability as zero, this may be construed to mean that the taxpayer has "paid income taxes under 15-30-103." The intent should be clarified by specifying that the taxpayer is subject to the surtax if the taxpayer *had no income tax liability* in the prior year. Further, "paid income taxes in the prior year" is unclear. Tax liabilities for tax year 2005 are often not paid until tax year 2006 when the return is filed; when are the taxes "paid"? Also, a taxpayer could "pay" a nominal amount of tax, and then claim a refund in subsequent years to avoid the surtax. Tying the surtax to a determination of positive tax liability associated with a specific tax year would facilitate and clarify the intent of the bill.
8. In administering the provisions of this bill, it would be necessary to provide county treasurers with information indicating whether or not a particular piece of residential property had or had not paid individual income taxes. Under current statutes this information is confidential. The bill may have to

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amend 15-30-303, MCA, to allow this information to be divulged to county treasurers or others that may need the information in order to effectively administer the provisions of the bill.